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C O N F I D E N T I A L SECTION 01 OF 04 BRUSSELS 000881

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STATE PASS TO USTR AND OIRA/OMB AND SEC
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SUBJECT: LUNCH SESSION OF TRANSATLANTIC ECONOMIC COUNCIL
(TEC) MAY 13, 2008

Classified By: Charge Christopher W. Murray for reasons 1.4 (b) and (d)

Participants:
U.S. Side

Dan Price, Assistant to the President for International
Economic Affairs, NSC
Ed Schafer, Secretary of Agriculture
Elaine Chao, Secretary of Labor
Susan Schwab, U.S. Trade Representative
Robert Kimmitt, Deputy Secretary of the Treasury
Reuben Jeffery, Under Secretary of State for Economic,
Energy, and Agricultural Affairs
Andrew Von Eschenbach, FDA Commissioner
Paul Atkins, Commissioner, Securities and Exchange Commission
[C](#). Boyden Gray, Special Envoy for EU Affairs
Susan Dudley, Administrator OIRA/OMB
John Herrmann, Special Assistant to the President and Senior
Director for International Trade, Energy, and the
Environment, NSC
Julie Nutter, Notetaker, U.S. Mission to the EU

EU Side

Guenter Verheguen, Commissioner for Enterprise and Industry
Peter Mandelson, Commissioner for Trade
Charlie McCreavy, Commissioner for Internal Market and
Services
Meglena Kuneva, Commissioner for Consumer Protection
Laszlo Kovacs, Commissioner for Taxation and Customs Union
Joaquin Almunia, Commissioner for Economic and Monetary
Affairs
Andrej Vizjak, Slovenian Economy Minister
Alan Seatter, Director, External Relations (RELEX)
John Farnell, Notetaker, Enterprise and Industry

[1](#)1. (C) Summary: At the May 13 U.S.-EU Transatlantic Economic Council meeting in Brussels, principals held a private lunch where they discussed how to combat protectionism, responses to food crises, biotechnology and biofuels, and our respective approaches to Russia. On combating protectionism, participants agreed that the U.S. and the EU should be alert to any use, particularly among emerging economic powers, of the pretexts of the economic downturn, food crises, the credit crunch, or negative responses to globalization to promote protectionism. On the links being made between food crises and biofuels production, several participants highlighted the need for policymakers to push back strongly,

citing the factual basis of food shortages, i.e., rising global demand for food and feed, and benefits of using biofuels. The TEC can help by promoting regulatory cooperation in biofuels and other energy-saving technologies.

Participants exchanged views on agricultural biotechnology as the best solution to food crises, and the U.S. side pointedly underlined their perception that negative attitudes on the part of some member states and some in the European Commission smacked of protectionism and had serious impacts on the ability of poorer countries to use biotech products to increase agricultural yields. On Russia, attendees varied in their assessment of Russian reform and the best path for the West to take; EU TEC co-chair Verheugen agreed to consult with U.S. counterparts upon his return from the June 18 EU-Russia Summit. End

Summary

Combating Protectionism

¶2. (U) EU Trade Commissioner Peter Mandelson led off the discussion on combating protectionism by noting that if the assessment that protectionism is rising "structurally" is correct, policymakers need to determine how to respond. To be sure, he said, those who currently advocate erecting protectionist barriers are speaking with more confidence, aided by global economic uncertainty; rising food and fuel prices; the stagnation of real wages in many countries; the challenge of climate change; louder demands for state intervention in economic matters; and a shift in relative economic power around the globe. Adding to these pressures,

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he noted, is a perception in some industrialized nations that emerging economic powers are shirking economic responsibility with impunity.

¶3. (SBU) That said, Mandelson continued, the US and the EU remain the world's largest economic powers, and as such share responsibility for economic leadership. To address some of the aforementioned concerns, transatlantic policymakers need to reiterate our commitment to economic liberalization; however, we also need to present stronger economic arguments for maintaining openness and to warn of the very real dangers of beggar-thy-neighbor policies. We need to promote a virtuous circle of liberalization, not a destructive cycle of closing. The NSC's Dan Price noted that in the U.S., some perceive globalization as benefiting only the elite, without a concomitant expansion of the social safety net for those who have been negatively affected. Price noted that policymakers now have to rebuild a constituency for globalization. As an analytical matter, he said, we have to separate trade protectionism from investment protectionism, since they are different phenomena with different origins.

¶4. (SBU) Mandelson posited that the U.S. and the EU would probably be more successful if we made a better case for reciprocity across the board, and in particular, if we were united on how we approach sovereign actors practicing state capitalism. The primary weakness the U.S. and the EU have in dealing with these state actors is that we do not currently have the strength of the multilateral system behind us to hold the emerging economies to account. That is why, he stated, the Doha Development Round is so important. Doha would not only enhance market access, its most obvious function, but it also would bind countries to openness, reducing the scope and space for future protectionism, be it protectionism targeted at trade or investment.

Food Crisis, Biotechnology and Biofuels

¶5. (C) Mandelson noted that the food crisis is a long-term structural issue, and warned that policymakers are more likely to get it wrong if they respond with panicky, short-term solutions rooted in protectionism. What the U.S. and the EU do not want to see is a global shift to managed

agricultural trade, despite what some EU member state agricultural ministers say (Comment: an explicit reference to the French and the German agriculture ministers). The longer-term answer, stressed Mandelson, is higher agricultural productivity in developing countries. Price commented that protectionist trends were strengthening before global food price increases came to a crisis point, but the food crisis has accentuated them. Regarding the need for higher agricultural productivity, Price observed that policymakers have mistakenly framed biotechnology as a trade issue only, when it is actually also a means to address a humanitarian need. President Bush wanted him to stress this point at the TEC, Price said. Agriculture Secretary Schafer underlined the fact that the cause of current food shortages is not commodity availability - globally, short-term supplies are still adequate - but in the longer-term, increasing consumption will demand higher yields. According to Schafer, the only countries in the world that are currently experiencing higher yields are (Comment: GMO-producing) Argentina, the U.S., and Canada.

16. (C) Commissioner Verheugen noted that in Europe, green biotechnology is highly ideological; the limits on production and consumption stem from societal preference rather than from protectionism. Secretary Schafer pointed out that when the EU tells Africans that Europe cannot import biotech products, it prevents Africans from importing seed to use to grow the crops that could have higher yields. Dan Price interjected that the effect of limiting trade in biotech products is ultimately protectionist and increasingly a food problem. USTR Schwab commented that French farmers made the decision to use biotech seeds that have a 10-year record of safety. There appears to be a "remarkable correlation" between regimes that are seriously protectionist and those with a history of hostility to biotech products, she noted. The key is educating the public. The TEC's risk assessment work could be helpful here. Internal Market Commissioner

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McCreavy said he thinks Irish farmers would plant GMO crops if they could, but the green lobby is "very difficult".

17. (SBU) On biofuels, Mandelson continued, proposals have been made to limit biofuels production or trade in order to protect domestic markets; the answer really lies in producing or using the most efficient biofuels. Targeting U.S. biofuels subsidies, Mandelson observed that if governments were to focus on orienting policies toward producing the right biofuels, subsidies would not be an issue. Verheugen reminded everyone that biofuels do not provide the only solution to the climate change problem; we must also increase energy efficiency, conservation, and use other means of lowering energy use. He characterized the biofuels debate as "already lost", since (specious) links have been made between food crises and biofuels production.

18. (SBU) Mandelson disagreed, saying he believes policymakers have not had the confidence to mount a persuasive counter-argument, and expressed the hope that the issue would be taken up in the G-8. Secretary Chao observed that Treasury Secretary Paulson had already raised the issue in a G-8 context, and the recent OECD Labor Ministers meeting had taken up the point as well. Special Envoy Gray pointed out that no one has highlighted the role of biofuels in lowering gasoline prices, and said the price of gasoline relative to crude oil is at an historic low in the U.S. Price noted that the prevailing wisdom on biofuels, i.e., that the production of biofuels consumes more energy than is saved by their use, has not been conclusively proven. We should "get the (positive) story out", he said, accelerate TEC work on biofuels standards with the Brazilians, and work for clean technologies in the TEC.

19. (SBU) On climate change, Mandelson opined that we need to approach the issue with a more integrated view of climate change and economic policy, and we need to involve all major

economies, with common but differentiated responsibilities. We should accomplish this, he stated, without resorting to trade-distorting measures such as border taxes. Price agreed, noting that he wants to include energy technologies in the TEC for one main reason - to ensure that economic and trade ministers, not just environment ministers, are discussing issues related to climate change.

Protectionism and Financial Services

¶10. (SBU) Commissioner McCreevy observed that sovereign wealth funds had actually helped to buoy the world economy during the credit crunch. He assessed that protectionist tendencies in financial services have diminished from a year ago, and commented that the financial crisis had actually lessened protectionist pressures by demonstrating the global economy's interdependence. Deputy Secretary Kimmitt noted that the transatlantic response to the credit crisis had been a "textbook case" of a measured reaction. Kimmitt added that he believes bilateral and multilateral cooperation in the crisis allowed for a diversity of solutions. On the question of the regulation of complicated financial instruments, Kimmitt said the sophistication of the products simply outstripped the ability of firms, rating agencies and regulators to adequately value underlying risk. However, Kimmitt noted, he sees robust evidence of a continued customer appetite for sophisticated financial products and investment in the U.S. financial sector, citing interest from Chinese banks.

¶11. (C) Commissioner McCreevy noted that it was largely regulated financial products that caused the biggest valuation headaches; thus, financial institutions will have to take a "hard look" at their policies and operations to determine what constitutes truly prudential regulation. Of course, he added, this also applies to third countries. There is a need for careful regulation, he said, but there will also be the temptation to use regulation as a tool for protecting sectors. The Chinese, for example, will have to walk a fine line, since what might be used to protect their financial sector could limit their access to innovative products. Price summed up the preceding conversation by noting that all agreed that U.S. and EU policymakers should

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keep alert to the use of any present exigencies, be it the food price crisis, climate change, or the economic slowdown, as pretexts to promote protectionism.

Russia

¶12. (C) U/S Jeffery introduced the topic of Russia, saying that the U.S. had recently re-invigorated its economic dialogue with the Government of Russia (GOR). In the dialogue discussions, which covered trade, Jackson-Vanik, investment, and energy, Jeffery said the Russians were, somewhat surprisingly, very focused on energy efficiency and renewables. However, U/S Jeffery noted that during the discussions the "elephants in the room" were the rule of law and energy security. In the business-to-business portion of the dialogue, Jeffery said, participants discussed the rise of Russian consumer influence (linked to economic growth), and internal "doing business" problems such as the business environment, property rights, the sanctity of contracts, and the corruption of the judicial system. Jeffery observed that the U.S. and the EU need to "draw Russia in" to encourage responsible behavior. Price noted the challenges in doing so, because Russian economic policymakers routinely use regulatory uncertainty to keep business and diplomatic partners off balance.

¶13. (C) Verheugen noted he would travel to Russia on June 14 for the EU-Russia summit, and that his trip could provide a good "test case" for assessing whether the GOR is acting responsibly. Verheugen underlined Russia's strategic importance for the EU, saying that as well as a crucial

source of energy, Russia is a lucrative market for EU companies. However, despite the current run of healthy profits, Verheugen said he foresees the day when the Russian economy is largely state-controlled. His conclusion is that the EU needs Russia more than in the past, but it needs Russia to be a predictable partner, and a stable, long-term relationship is not possible without an alignment of values. Commissioner Kovacs made the point that the West should not make the mistake of allowing the Russians to think they will regain superpower status, or regain control over parts of its former empire, whether in eastern Europe or in Central Asia.

¶14. (C) Mandelson surmised that Russia is increasingly autocratic because it has large financial inflows from energy and counts on the energy dependence of its neighbors. But, Mandelson continued, these resources are finite, and the West must reach out to those in Russia who recognize that. Russia will need investment and high-tech to grow and to diversify its economy, and it will naturally turn to Europe and the U.S. Thus, Russia's future lies in reform. Mandelson said he believes that Medvedev is an economic liberal and will probably accept needed economic changes, as well as improvements to the rule of law. Mandelson said he is encouraged by some of Medvedev's recent appointments, notably the chief WTO negotiator and the head of the Presidential Administration, as well as some of his appointees at the Justice Ministry. Mandelson said he believes economic opening will help promote political opening, and that Russia "will outgrow Putin."

¶15. (C) Verheugen said he thought what the Russians want above all is respect. Price added that while we treat them with respect, we should also test their receptivity to political and economic opening and not give them the impression that we are lowering our expectations on reform and accountability. Mandelson said he believes the Russians are apt to take advantage of the end of the U.S. Administration to put pressure on the "near abroad". Deputy Secretary Kimmitt countered by saying he thought a successor U.S. administration would be even firmer on Russia. The group agreed to consult informally upon Verheugen's return from Moscow.

Murray

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